

Internal Revenue Service

Number: **201203011**

Release Date: 1/20/2012

Index Number: 1362.04-00, 1362.01-03,
1361.03-02

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:02

PLR-117930-11

Date:

October 17, 2011

LEGEND

X =

State =

A =

B =

C =

Trust 1 =

Trust 2 =

Trust 3 =

Date 1 =

Date 2 =

Date 3 =

Date 4 =

Date 5 =

Date 6 =

Date 7 =

Date 8 =

Date 9 =

a =

b =

Dear :

This responds to a letter dated April 11, 2011 and subsequent correspondence submitted on behalf of X by X's authorized representative, requesting relief under section 1362(f) of the Internal Revenue Code.

FACTS

According to the information submitted, X was incorporated on Date 1 under the laws of State. X timely elected to be an S Corporation effective Date 2. Over time, A acquired all outstanding shares of X. A transferred those shares to Trust 1 on Date 3. Trust 1 was a revocable trust treated as a wholly-owned grantor trust under § 671 and 676 until A's death on Date 9. On Date 4, A created two irrevocable trusts, Trust 2 and Trust 3. B is the sole beneficiary of Trust 2. C is the sole beneficiary of Trust 3.

On Date 5, A transferred a shares of X to Trust 2 and a shares of X to Trust 3. On Date 6, A transferred a shares of X to Trust 2 and a shares of X to Trust 3. On Date 7, A transferred b shares of X to Trust 2 and b shares of X to Trust 3. On Date 8, A transferred b shares of X to Trust 2 and b shares of X to Trust 3.

X represents that Trust 2 and Trust 3 were eligible at all times to be treated as qualified subchapter S trusts (QSSTs) under § 1361(d)(3). B and C failed to make timely QSST elections causing the termination of X's S corporation status on Date 5.

X represents that the circumstances resulting in the termination of X's S corporation election were inadvertent and not motivated by tax avoidance. X represents that from Date 2, X and its shareholders filed federal income tax returns consistent with X's status as an S corporation election. X further represents that from Date 5, B and C consistently filed their income tax returns as if Trust 2 and Trust 3 had valid QSST elections in effect. X and its shareholders consent to make any adjustments, consistent with the treatment of X as an S corporation, as may be required by the Secretary.

LAW

Section 1361(a)(1) defines an "S corporation" as a small business corporation for which an election under § 1362(a) is in effect for the taxable year.

Section 1361(b)(1)(B) defines a "small business corporation" as a domestic corporation which is not an ineligible corporation and which does not (A) have more than 100 shareholders, (B) have as a shareholder a person (other than an estate and other than a trust described in § 1361(c)(2) or an organization described in § 1361(c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than 1 class of stock.

Section 1361(d) provides that a QSST whose beneficiary makes an election under § 1362(d)(2) will be treated as a trust described in § 1361(c)(2)(A)(i), and the QSST's beneficiary will be treated as the owner (for purposes of § 678(a)) of that portion of the QSST's S corporation stock to which the election under § 1361(d)(2) applies.

Section 1361(d)(3)(A) provides that for purposes of § 1361(d), the term "qualified subchapter S trust" means a trust, the terms of which require that — (i) during the life of the current income beneficiary, there shall be only 1 income beneficiary of the trust; (ii) any corpus distributed during the life of the current beneficiary may be distributed only to such beneficiary; (iii) the interest of the current income beneficiary in the trust shall terminate on the earlier of such beneficiary's death or the termination of the trust; and (iv) upon the termination of the trust during the life of the current income beneficiary, the trust shall distribute all of its assets to that beneficiary. Section 1361(d)(3)(B) requires the trust to distribute all of its income (within the meaning of § 643(b)) to 1 individual who is a citizen or resident of the United States.

Section 1362(f) provides, in relevant part, that if (1) an election under § 1362(a) by any corporation (A) was not effective for the taxable year for which it was made (determined without regard to § 1362(b)(2)) by reason of a failure to meet the requirements of § 1361(b) or to obtain shareholder consents, or (B) was terminated under § 1362(d)(2) or (3); (2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent; (3) no later than a reasonable period of time after discovery of the event resulting in the ineffectiveness of termination,

steps were taken (A) so that the corporation is a small business corporation, or (B) to acquire the required shareholder consents; and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to § 1362(f), agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period, then, notwithstanding the circumstances resulting in such ineffectiveness or termination, the corporation shall be treated as an S corporation during the period specified by the Secretary.

CONCLUSION

Based solely on the facts submitted and the representations made, we conclude that X's S corporation election terminated on Date 5 because Trust 2 and Trust 3 were not eligible shareholders of X. We also conclude that the termination of X's S election on Date 5 was an inadvertent termination within the meaning of § 1362(f). Therefore, X will be treated as an S corporation effective Date 2 and thereafter, provided X's S corporation election is not otherwise terminated under § 1362(d).

This ruling is contingent upon B and C filing QSST elections for Trust 2 and Trust 3, respectively, with an effective date of Date 5 with the appropriate service center within 60 days of the date of this ruling. A copy of this letter should be attached to each election.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, no opinion is expressed regarding X's eligibility to be an S corporation or the validity of its S corporation election. No opinion is expressed as to whether Trust 1 is a permissible S corporation shareholder or whether Trust 2 or Trust 3 qualifies as a QSST.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Melissa C. Liquerman
Branch Chief, Branch 2
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures (2)
Copy of this Letter
Copy for § 6110 purposes